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Lakson Tobacco Company Ltd

Analysis of Financial Statements

FY03 — Q3FY09

The tobacco industry in Pakistan is oligopolistic in nature with two major players in the market; both belonging to the organized sector and a few minor players in the organized d many in the unorganized sector. The Lakson tobacco company a part of the Lakson Group which was founded in 1954. The mpany's major activity is the manufacture and sale of cigarettes Pakistan. It is a publicly listed corporation and is the largest bacco exporter in Pakistan. The Company operates in five facto-s located in Karachi in the districts of Dadu, Sahiwal, walpindi and Swabi.

Lakson tobacco's leading brands include Morven Gold along th Red and White. Lakson Tobacco is Pakistan's second largest bacco company, with an estimated cigarette volume of 29.8 bil-n units in fiscal year, ending 30 June, 2006. in the FY'06 the mpany held an estimated 47% share of the growing 63 billion-it Pakistan cigarette market. In March 2007, Phillip Morris ernational acquired an additional 50.21% stake in Lakson bacco Company to bring its share in the Tobacco Company to proximately 90%.

Lakson Tobacco's main brands, include :

Park Lane
Premier Classic
Red & White
Morven Gold
Princeton
K2, and
Diplomat

Times Interest Earned

kson Tobacco Company has shown decent growth rates over years. In 2005 the company performed exceedingly well and able to achieve growth in all areas. Its operating profits were higher than the Same Period Last Year (SPLY). This oved performance can be attributed to higher sales volume, oved margins, better brand mix and control over cost through on operational efficiencies. However the Company could not tain its superb performance of 2005 in 2006 as the sales were ame as last year and operating profit declined by 7.4% over Same Period Last Year (SPLY). In 2007 the company oved its performance over the 2006 performance and ased Sales by 9%, Gross Profit 8% and operating profit 12% ite of an 8% increase in the cost of sales due to a 15 % ase in the prices of tobacco.

FY 09 Review

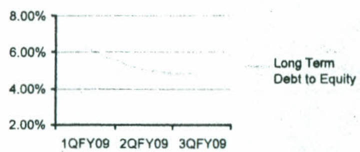
ring the nine months under review, the Company's turnover ased by 22.2% to be Rs. 22.1 billion as compared to Rs. 18.34 n the same period last year. Lakson's gross profit increased .3% to be Rs. 3.72 billion. However, the gross profit margin ome down to 16.6% as compared to 17.6% in the same peri-it year. Cost of production has increased greatly in line with onary pressures prevailing over the economy. Overall distri-, marketing and administrative expenses increased by 53.2% increased marketing activities and higher employee's com-tion. Other operating expenses decreased by 18.7%. The net decreased by 20.8% to be Rs. 862 million as compared to

TIE ratio has deteriorated due to rising financial charges and reduced PAT. Although there is no significant Long term debt, short term financing has increased.

FY08

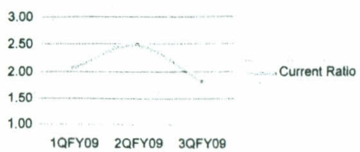
Note (The Company has changes its year end from June to December and therefore the comparison made at places will be of full year FY08 with six month period ending at December 31, 2008 as according to the financial statements released by the company and at some places according to full year FY07 which have been estimated by the six month figures given in the financial statements).

Long Term Debt to Equity



The company performance remained unsatisfactory in FY08 this because of a tough first and third quarter in the current year. The company had suffered huge losses due to the December 27, 2007 riots resulted in significant losses and damages to the Company's assets (both human and property) at Korangi Industrial Area. The company also eliminated the services of its employees on 4th April with one month pay as it was not in a position to resume its manufacturing operations which requires a significant investment for installing new plant, machinery, equipment and incurring costs relating to the civil works. However the company which has been among the top 25 company's at the KSE in 2006 and 2007 could not maintain its 2007 performance as it faced difficult times due to sharp decline in the demand for tobacco which has decreased from 79 million kilograms in the year 2007 to 71 million kilograms currently which adversely affected the Companies profitability. Apart from this the deteriorating economic conditions, inflation, load shedding and the sharp rupee depreciation during the period had also added to the difficulties.

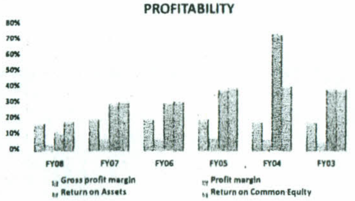
Current Ratio



The net turnover of Lakson Tobacco Company was 16%

which increased due to an increase in the wages paid and also due to an increase in Purchases and redrying expenses which increased due to an increase in the cost of raw materials. The cost of sales to net turnover ratio decreased by 0.97% as compared to the last period which reveals measures taken by the management to improve the efficiency in the business. The company also managed to keep a check on its expenses over the year despite a huge increase in its distribution and marketing expense and in the administrative expense in the 3rd quarter of the current fiscal year. The company's distribution and marketing expense increased by 8% as compared to the estimated FY07 expense. This was due to an increase in the cost of sponsorship and event marketing. The company also had a 31% increase in its administrative expense due to an increase in the wages expense. The company had a 30% increase in it's before tax profit but due to a 60% increase in the taxes paid the company's after tax profit were limited to a 16% increase over the Same Period Last Year (SPLY). This year the Company contributed Rs 14.7 billion to the national exchequer in the form of Federal Excise Duty, Sales Tax, Custom Duties, and Income Tax etc. This was also due to an increase in GST to 16% during the year.

PROFITABILITY



The Company maintained its gross profit in FY08 as compared to the last six months of FY07 with the Gross profit being close to 17.5%. The company could not increase its Gross Profit Margins due to increase in cost of sales due to rising inflation. The company's Gross Profit Margins were similar to its major competitor Pakistan Tobacco Company (PTC) which had Margins of approximately 18% during the 9MFY08. The company's profitability margin declined slightly from 4.59% in the last six months of FY07 to 4.43% in FY08. The profitability margins were lower than its major competitor Pakistan Tobacco Company (PTC) which had a profitability margin of 6.8% which was due to higher distribution and marketing expenses. Thus, in spite of having the same gross profit as PTC the company's profit margin were lower which shows that there is a need to control its cost base. The company's return on assets (ROA) was 11.71% in FY08 as compared to 6.08% in the last six months of FY07 and the company's return on equity (ROE) improved to 18.44% from 8.55% in the last six months of FY07.

The company's liquidity position worsened slightly as its Current Ratio decreased from 2.56 in FY08 to 1.99 in the last six

among the industry. Its Current Ratio was 1.99 in FY08 as compared to 0.95 for PTC during 9MFY08.

The company's interest coverage ratio declined from 80 in the last six months of FY07 to 39.24 in FY08 due to a 439% increase in the finance cost. The company's debt to assets ratio was 6.55% in FY08 as compared to 5.66% in FY07.

The company's earning per share is higher than that of other Tobacco company's in the industry. The company's earning per share was Rs.17.95 in FY08 as compared to Rs.7.65 in the last six months of FY07. The company's book value also improved from Rs.55.1 at the end of FY07 to Rs.60 at the end of FY08.

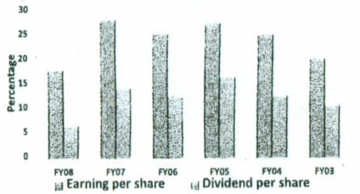
CURRENT RATIO

Future Outlook

LTC is a fully integrated affiliate of Philip Morris International and wants to improve its utilization of global resources to accelerate superior performance in all areas. The Management wants to bring an improvement in all areas of its operations through innovative marketing, upgrading of plant and machinery, development of human capital and continued emphasis on cost control especially its distribution and administrative cost.

The company however faces significant challenges which include the recommendation by the Senate body on March 9th 2009 to raise the prices of tobacco leaf (which cigarette manufacturers buy from growers) to Rs.150/kg. This was because the Senate body found the crop price to be grossly undervalued and agreed with the farmer's view of surge in their input cost like fertilizer and overall impact of double digit rise in inflation. If this is implemented this would mean an increase of 83% over the Rs.82 price suggested by the Pakistan tobacco board (PTB) and could significantly impact the profitability of the company which would further have to improve its cost control.

Market Value



Economics and Finance Department, Institute of Business Administration, Karachi, prepared this analytical report for Business Recorder.

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